

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

**Basic Financial Statements
and Supplementary Information
June 30, 2012 and 2011**

Together with Independent Auditor's Report

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

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Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Officials
June 30, 2012

| | Address | Term Expires |
|--|----------------|---------------------|
| Board of Trustees: | | |
| Matt Hummel, President | Hawarden, Iowa | December 2015 |
| Kathy Jacobs, Vice-President | Hawarden, Iowa | December 2015 |
| Glea Hamik, Secretary | Hawarden, Iowa | December 2015 |
| Denny Hulshof | Ireton, Iowa | December 2013 |
| Stan Hoekstra | Hawarden, Iowa | December 2013 |
| Hospital Officials: | | |
| Jayson Pullman – Chief Executive Officer | Hawarden, Iowa | Indefinite |

Independent Auditor's Report

To the Board of Trustees
Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
Hawarden, Iowa:

We have audited the accompanying basic financial statements of Hawarden Regional Healthcare (f/k/a Hawarden Community Hospital) (Hospital), a component unit of the City of Hawarden, Iowa, as of and for the years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards and provisions require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As explained in Note 1, the accompanying financial statements present only the Hospital Fund of the city of Hawarden, Iowa, and are not intended to present fairly the financial position of the city of Hawarden, Iowa, and the results of its operations, changes in fund balance and its cash flows in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hawarden Regional Healthcare as of June 30, 2012 and 2011, and the results of its operations, changes in net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 25, 2012 on our consideration of the Hospital's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of the report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole. The other supplementary statements (Exhibits 1 – 6) are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 25, 2012.

Management's Discussion and Analysis **June 30, 2012 and 2011**

Our discussion and analysis of Hawarden Regional Healthcare's (f/k/a Hawarden Community Hospital) financial performance provides an overview of the Hospital's financial activities for the fiscal years ended June 30, 2012 and 2011. Please read it in conjunction with the Hospital's financial statements, which begin on page 7.

Financial Highlights

- The Hospital's net assets increased in each of the past two years with a \$1,025,543 or a 27.1% in 2012 and a \$496,876 or a 15.1% in 2011.
- The Hospital reported operating income in 2012 of \$727,521 which was a \$484,162 increase from 2011 operating income of \$243,359. The operating income in 2011 increased by \$333,168 or 371% from the loss reported in 2010 of \$(89,809).
- Operating revenues increased by \$1,437,254 or 21.9% over the revenues reported in 2011. 2011 operating revenue increased by \$603,817 or 10.2% over the revenues reported in 2010.
- Nonoperating revenues and restricted gifts received increased by \$44,505 or 17.6% in 2012 compared to 2011 and a decrease of \$(57,223) or 18.4% in 2011 compared to 2010.

Using This Annual Report

The Hospital's financial statements consist of three statements; a Balance Sheet; a Statement of Revenue, Expenses, and Changes in Net Assets; and a Statement of Cash Flows. These financial statements and related notes provide information about the activities of the Hospital, including resources held by the Hospital but restricted for specific purposes by contributors, grantors, or enabling legislation.

The Balance Sheet and Statement of Revenue, Expenses, and Changes in Net Assets

Our analysis of the Hospital finances begins on page 4. The Balance Sheet and the Statement of Revenue, Expenses, and Changes in Net Assets report information about the Hospital's resources and its activities in a way that helps answer the question of whether the Hospital, as a whole, is better or worse off as a result of the year's activities. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenue and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net assets and changes in them. You can think of the Hospital's net assets, the difference between assets and liabilities, as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Hospital.

The Statement of Cash Flows

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It shows where cash came from and what the cash was used for. It also provides the change in cash balance during the reporting period.

The Hospital's Net Assets

The Hospital's net assets are the difference between its assets and liabilities reported in the Balance Sheet on page 7. The Hospital's net assets increased in each of the past two years by \$1,025,543 (27.1%) in 2012 and \$496,876 (15.1%) in 2011, as you can see from **Table 1**.

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Management's Discussion and Analysis
June 30, 2012 and 2011

Table 1: Assets, Liabilities, and Net Assets

| | <u>2012</u> | <u>2011</u> | <u>2010</u> |
|--|----------------------------|-------------------------|-------------------------|
| Assets: | | | |
| Current assets | \$ 4,595,615 | 3,134,479 | 2,417,236 |
| Capital assets, net | 1,389,486 | 1,394,084 | 1,279,500 |
| Other noncurrent assets | 546,361 | 485,128 | 733,886 |
| Total assets | \$ <u>6,531,462</u> | <u>5,013,691</u> | <u>4,430,622</u> |
| Liabilities: | | | |
| Long-term debt outstanding | \$ -- | -- | 224,466 |
| Other current and noncurrent liabilities | 1,718,089 | 1,225,861 | 915,202 |
| Total liabilities | \$ <u>1,718,089</u> | <u>1,225,861</u> | <u>1,139,668</u> |
| Net assets: | | | |
| Invested in capital assets, net of related debt | \$ 1,389,486 | 1,394,084 | 1,055,034 |
| Expendable for capital acquisitions and operating activities | 67,157 | 75,177 | 104,421 |
| Nonexpendable permanent endowments | 96,123 | 96,123 | 96,123 |
| Unrestricted | 3,260,607 | 2,222,446 | 2,035,376 |
| Total net assets | \$ <u>4,813,373</u> | <u>3,787,830</u> | <u>3,290,954</u> |

In 2012, the total assets increased by \$1,517,771. A significant component of the change is an increase in the accounts receivable due from patients. The increase in patient volumes was a contributing factor. Cash and cash equivalents were also a huge part of this as more patient revenues were collected during 2012.

In 2012, the total liabilities increased by \$492,228. The change was primarily due to the estimated third party payor settlements.

Operating Results and Changes in The Hospital's Net Assets

In 2012, the Hospital's net assets increased by \$1,025,543 (27.1%), as shown in **Table 2**. This increase is made up of very different components.

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Management's Discussion and Analysis
June 30, 2012 and 2011

Table 2: Condensed Statements of Revenues, Expenses and Changes in Net Assets

| | 2012 | 2011 | 2010 |
|---|---------------------|------------------|------------------|
| Operating Revenue: | | | |
| Net patient service revenue | \$ 7,255,445 | 5,850,066 | 5,160,940 |
| Provision for bad debt | (602,900) | (723,480) | (204,560) |
| Other operating revenues | 723,729 | 691,854 | 777,163 |
| Total operating revenue | 7,376,274 | 5,818,440 | 5,733,543 |
| Operating Expenses: | | | |
| Salaries and benefits | 2,915,654 | 2,627,734 | 2,434,299 |
| Purchased services and other | 3,478,284 | 3,135,592 | 3,155,880 |
| Depreciation and amortization | 254,144 | 324,428 | 297,674 |
| Interest | 671 | 6,247 | 16,559 |
| Total operating expenses | 6,648,753 | 6,094,001 | 5,904,412 |
| Operating income (loss) | 727,521 | (275,561) | (170,869) |
| Nonoperating Revenues (Expenses) | | | |
| Joint venture and clinic investment loss, net | (15,085) | (122,864) | (71,617) |
| Gain on sale of property and equipment | -- | -- | 1,100 |
| Investment income | 12,310 | 21,353 | 23,900 |
| Sales tax revenue | 278,233 | 278,820 | 258,303 |
| Gifts, grants and contributions, net | 22,564 | 76,208 | 99,054 |
| Total nonoperating revenue (expenses), net | 298,022 | 253,517 | 310,740 |
| Increase in net assets | 1,025,543 | (22,044) | 139,871 |
| Net assets beginning of year | 3,187,850 | 3,209,894 | 3,070,023 |
| Net assets end of year | \$ 4,213,393 | 3,187,850 | 3,209,894 |

Nonoperating Revenues and Expenses

Nonoperating revenues consist primarily of local option sales taxes, interest revenue, investment earnings and gifts, grants and bequests for the purchase of property and equipment.

The loss for the joint venture and clinic investment was \$(15,085) in 2012 compared to \$(122,864) in 2011. We continue to fund the clinic as part of our mission to provide for the health and wellness of all the people in our community.

Management's Discussion and Analysis
June 30, 2012 and 2011

The Hospital's Cash Flows

Changes in the Hospital's cash flows are consistent with changes in operating income and nonoperating revenues and expenses, discussed earlier. Cash flows provided by operating activities in 2012 increased compared to 2011 due to an increase in cash received from patients and third party payors.

Capital Asset and Debt Administration

Capital Assets

As of end of the year 2012, the Hospital had \$1,389,486 invested in capital assets, net of accumulated depreciation, as compared to \$1,394,084 in 2011 and \$1,279,500 in 2010, as detailed in Note 7 of the financial statements. In 2012, the hospital purchased depreciable capital assets costing \$249,54 compared to \$465,220 being spent in 2011. The hospital purchased computer system upgrades for \$113,961, patient elevator repairs \$58,289, hospital expansion costs \$9,164, surgery equipment \$13,250, inpatient bed \$5,496, and telephone system upgrades \$49,386.

Debt

As of end of the year 2012, the Hospital had no loans or capital lease obligations outstanding. The Hospital also had no loans and capital lease obligations outstanding at year end 2011. No new loans were made in 2012. The Hospital's formal debt issuances, revenue notes, cannot be issued without approval of the Board of Directors.

Contacting the Hospital's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the CEO, at Hawarden Regional Healthcare, 1111 11th Street, Hawarden, Iowa 51023.

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Balance Sheets
June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|--|---------------------|------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 2,331,506 | 1,362,443 |
| Receivables - | | |
| Patients, net of allowance for doubtful accounts of | | |
| \$808,619 in 2012 and \$276,786 in 2011 | 1,491,040 | 919,973 |
| Due from related party | 411,064 | 552,234 |
| Other | 168,145 | 114,687 |
| Inventories | 103,951 | 80,598 |
| Prepaid expenses | 89,909 | 104,544 |
| | <u>4,595,615</u> | <u>3,134,479</u> |
| Assets limited as to use - | | |
| By board for capital improvements and endowments | 441,605 | 378,398 |
| By donor | 99,973 | 99,846 |
| | <u>541,578</u> | <u>478,244</u> |
| Capital assets, net | <u>1,389,486</u> | <u>1,394,084</u> |
| Other assets | <u>4,783</u> | <u>6,884</u> |
| Total assets | <u>\$ 6,531,462</u> | <u>5,013,691</u> |
| LIABILITIES AND NET ASSETS | | |
| Current liabilities: | | |
| Accounts payable - | | |
| Mercy | \$ 54,487 | 56,163 |
| Trade | 115,348 | 141,345 |
| Salaries, wages and accrued benefits payable | 176,315 | 232,734 |
| Payroll taxes withheld and accrued | 47,263 | 28,178 |
| Other accrued liabilities | 103,942 | 59,932 |
| Estimated third-party payor settlements | 1,220,734 | 707,509 |
| | <u>1,718,089</u> | <u>1,225,861</u> |
| Net assets: | | |
| Invested in capital assets, net of related debt | 1,389,486 | 1,394,084 |
| Restricted: | | |
| Expendable for capital acquisitions and operating activities | 67,157 | 75,177 |
| Nonexpendable permanent endowments | 96,123 | 96,123 |
| Unrestricted | <u>3,260,607</u> | <u>2,222,446</u> |
| Total net assets | <u>4,813,373</u> | <u>3,787,830</u> |
| Total liabilities and net assets | <u>\$ 6,531,462</u> | <u>5,013,691</u> |

See notes to financial statements

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Statements of Revenue, Expenses and Changes in Net Assets
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|---|---------------------|------------------|
| UNRESTRICTED REVENUE: | | |
| Net patient service revenue before provision for bad debt | \$ 7,255,445 | 5,850,066 |
| Provision for bad debts | <u>(602,900)</u> | <u>(204,560)</u> |
| Net patient service revenue | 6,652,545 | 5,645,506 |
| Other revenue | <u>723,729</u> | <u>691,854</u> |
| Total revenue | <u>7,376,274</u> | <u>6,337,360</u> |
| EXPENSES: | | |
| Salaries | 2,268,747 | 2,064,824 |
| Employee benefits | 646,907 | 562,910 |
| Purchased services and professional fees | 2,153,555 | 2,088,347 |
| Utilities | 71,859 | 83,272 |
| Supplies and other expenses | 1,182,501 | 900,543 |
| Depreciation | 254,144 | 324,428 |
| Insurance | 70,369 | 63,430 |
| Interest | <u>671</u> | <u>6,247</u> |
| Total expenses | <u>6,648,753</u> | <u>6,094,001</u> |
| OPERATING GAIN | <u>727,521</u> | <u>243,359</u> |
| NONOPERATING GAINS (LOSSES), NET: | | |
| Joint venture and clinic investment loss, net | (15,085) | (122,864) |
| Investment income | 12,310 | 21,353 |
| Sales tax revenue | 278,233 | 278,820 |
| Noncapital grants and contributions | <u>20,861</u> | <u>25,000</u> |
| Nonoperating gains, net | <u>296,319</u> | <u>202,309</u> |
| EXCESS OF REVENUE OVER EXPENSES | 1,023,840 | 445,668 |
| CAPITAL GRANTS AND CONTRIBUTIONS, NET | <u>1,703</u> | <u>51,208</u> |
| INCREASE IN NET ASSETS | 1,025,543 | 496,876 |
| NET ASSETS, BEGINNING OF YEAR | <u>3,787,830</u> | <u>3,290,954</u> |
| NET ASSETS, END OF YEAR | <u>\$ 4,813,373</u> | <u>3,787,830</u> |

See notes to financial statements

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Statements of Cash Flows
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|---|----------------------------|-------------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Cash received from patients and third party payors | \$ 6,594,703 | 5,786,789 |
| Cash paid for employee salaries and benefits | (2,952,988) | (2,613,600) |
| Cash paid to suppliers and contractors | (3,524,123) | (3,177,785) |
| Other receipts and payments, net | <u>864,899</u> | <u>516,598</u> |
| Net cash provided by operating activities | <u>982,491</u> | <u>512,002</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES: | | |
| Sales tax received | 278,233 | 278,820 |
| Noncapital grants and contributions | <u>20,861</u> | <u>25,000</u> |
| Net cash provided by noncapital financing activities | <u>299,094</u> | <u>303,820</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES: | | |
| Purchase of property and equipment, net | (249,546) | (452,720) |
| Capital grants and contributions | 1,703 | 51,208 |
| Payments on long-term debt | -- | (224,466) |
| Interest paid on long-term debt and capital lease obligations | <u>(671)</u> | <u>(6,247)</u> |
| Net cash used in capital and related financing activities | <u>(248,514)</u> | <u>(632,225)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Joint venture and clinic investment loss, net | (15,085) | (122,864) |
| Withdrawals from (deposits to) assets limited as to use | (63,334) | 251,294 |
| Investment income | 12,310 | 21,353 |
| Deposits (withdrawals) to other assets | <u>2,101</u> | <u>(2,536)</u> |
| Net cash provided by (used in) investing activities | <u>(64,008)</u> | <u>147,247</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 969,063 | 330,844 |
| CASH AND CASH EQUIVALENTS - Beginning of year | <u>1,362,443</u> | <u>1,031,599</u> |
| CASH AND CASH EQUIVALENTS - End of year | <u><u>\$ 2,331,506</u></u> | <u><u>1,362,443</u></u> |

See notes to financial statements

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Statements of Cash Flows (Continued)
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|--|-------------------|----------------|
| RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES: | | |
| Operating gain | \$ 727,521 | 243,359 |
| Adjustments to reconcile operating gain to net cash provided by operating activities - | | |
| Depreciation | 254,144 | 324,428 |
| Interest expense | 671 | 6,247 |
| (Increase) decrease in current assets - | | |
| Receivables - | | |
| Patients | (571,067) | (168,033) |
| Due from related party | 141,170 | (175,256) |
| Other | (53,458) | (765) |
| Inventories | (23,353) | (16,008) |
| Prepaid expenses | 14,635 | (26,337) |
| Increase (decrease) in current liabilities - | | |
| Accounts payable - | | |
| Mercy | (1,676) | (48,936) |
| Trade | (25,997) | 18,733 |
| Salaries, wages and accrued benefits payable | (56,419) | 9,745 |
| Payroll taxes withheld and accrued | 19,085 | 4,389 |
| Other accrued liabilities | 44,010 | 31,120 |
| Estimated third-party payor settlements | 513,225 | 309,316 |
| Net cash provided by operating activities | <u>\$ 982,491</u> | <u>512,002</u> |

See notes to financial statements

Notes to Financial Statements
June 30, 2012 and 2011

(1) Description of Reporting Entity and Summary of Significant Accounting Policies

The following is a summary of significant accounting policies of Hawarden Regional Healthcare (f/k/a Hawarden Community Hospital) (Hospital). These policies are in accordance with accounting principles generally accepted in the United States of America. The Hospital is a city public hospital organized under Chapter 392 of the Code of Iowa and governed by a five member Board of Trustees elected for terms of four years.

A. Reporting Entity

The financial statements of the Hospital are used to account for the provisions of acute hospital and physician clinic services to the residents of the City of Hawarden and the surrounding area.

The Hospital's financial statements are an integral part of the City of Hawarden, Iowa. The accompanying financial statements are not intended to present fairly the financial position and changes in financial position of the City of Hawarden, Iowa, in conformity with accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Hospital has included all funds, organizations, account groups, agencies, boards, commissions and authorities. The Hospital has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Hospital are such that exclusion would cause the Hospital's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Hospital to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Hospital. The Hospital has no component units which meet the Governmental Accounting Standards Board criteria.

The Budget Reconciliation Act of 1997 (Act) contained many provisions impacting Medicare reimbursement for Health Services. The Act established the Medicare Rural Hospital Flexibility Program to assist states and rural communities to improve access to essential health care services through limited service hospitals and rural health networks. During fiscal year 2000, the Hawarden Community Hospital Board of Trustees approved the Health Services' plan to obtain Critical Access Hospital (CAH) designation. CAH's are acute care facilities that provide emergency, outpatient and short-term inpatient services. Medicare reimburses CAH's on a reasonable cost basis.

The Hospital's application to become certified as a CAH was approved by the Iowa Department of Public Health and the certification was effective November 2, 2000.

B. Industry Environment

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursements for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Management believes that the Hospital is in compliance with government laws and regulations as they apply to the areas of fraud and abuse. While no regulatory inquiries have been made which are expected to have a material effect on the Hospital's financial statements, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

Notes to Financial Statements
June 30, 2012 and 2011

As a result of recently enacted federal healthcare reform legislation, substantial changes are anticipated in the United States healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement of healthcare providers and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over approximately the next decade.

C. *Basis of Presentation*

The balance sheet displays the Hospital's assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes and other debt attributable to the acquisition, construction or improvement of those assets.

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets not meeting the definition of the two preceding categories. Unrestricted net assets often have constraints on resources imposed by management which can be removed or modified.

When both restricted and unrestricted resources are available for use, generally it is the Hospital's policy to use restricted resources first.

D. *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

E. *Measurement Focus and Basis of Accounting*

Measurement focus refers to when revenue and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Revenue is recognized when earned and expenses are recorded when the liability is incurred.

Pursuant to Section 1600 of the Governmental Accounting Standards Board's (GASB) Codification of Governmental Accounting and Financial Reporting Standards, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

F. *Cash and Cash Equivalents*

Cash and cash equivalents for purposes of the statements of cash flows include investments in highly liquid debt instruments with original maturities of three months or less.

Notes to Financial Statements
June 30, 2012 and 2011

G. Patient Receivables, Net

Net patient receivables are uncollateralized customer and third-party payor obligations. Unpaid patient receivables are not assessed interest.

Payments of patient receivables are allocated to the specific claim identified on the remittance advice or, if unspecified, are applied to the earliest unpaid claim.

The carrying amount of patient receivables is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected from patients and third-party payors. Management reviews patient receivables by payor class and applies percentages to determine estimated amounts that will not be collected from third parties under contractual agreements and amounts that will not be collected from patients due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision.

H. Inventories

Inventories are stated at the lower of cost, determined by the first-in, first-out method, or market.

I. Assets Limited as to Use

By Board of Trustees - Periodically, the Hospital's Board of Trustees has set aside assets for future capital improvements and endowments. The Board retains control over these assets and may, at its discretion, subsequently use them for other purposes.

By Donor – These funds are restricted for specified purposes as directed by the grantor or donor.

J. Fair Value of Financial Instruments

The carrying value of all financial instruments approximates estimated fair value. Cash and cash equivalents, assets limited as to use, accounts receivable, and accounts payable approximate fair value due to the relatively short period of time between their origination and expected realization.

K. Capital Assets

Capital asset acquisitions in excess of \$5,000 are capitalized and recorded at cost. Depreciation is provided over the estimated life of each depreciable asset and is computed using the straight-line method.

Useful lives are determined using guidelines from the American Hospital Association Guide for Estimated Useful Lives of Depreciable Hospital Assets. Lives range by capital asset classification as follows:

| | |
|-------------------------------------|----------------|
| Land improvements | 10 to 50 years |
| Buildings and building improvements | 10 to 50 years |
| Equipment, computers, and furniture | 3 to 25 years |

The Hospital's long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected cash flows is less than the carrying amount of the asset, a loss is recognized.

Notes to Financial Statements
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Gifts of long-lived assets such as land, buildings or equipment are reported as unrestricted support and are excluded from the excess of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed into service.

L. Compensated Absences

Paid time off (PTO) vests and may be carried forward by an employee in an amount not to exceed 240 hours. PTO expense is accrued as an expense and a liability as it is earned. PTO expenditures are recognized to the extent it is paid during the year and the vested amount is recorded as a current liability. Accrued PTO payable at June 30, 2012 and 2011 was \$131,369 and \$124,007, respectively.

M. Statement of Revenue, Expenses and Changes in Net Assets

For purposes of display, transactions deemed by management to be on-going, major or central to the provision of health care services are reported as operating revenue and expenses. Peripheral or incidental transactions are reported as nonoperating gains and losses.

N. Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

O. Grants and Contributions

From time to time, the Hospital receives grants and contributions from individuals and private organizations. Revenue from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenue. Amounts restricted to capital acquisitions are reported after nonoperating revenue and expenses.

P. Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Q. Sales Tax Revenue

Taxes are included in nonoperating gains when received and distributed by the City Treasurer. No provision is made in the financial statements for taxes levied in the current year to be collected in a subsequent year.

R. Income Taxes

Under the Code of Iowa, Chapter 392, the Hospital is an instrumentality of the City of Hawarden, Iowa. As such, the Hospital is exempt from paying income taxes.

Notes to Financial Statements
June 30, 2012 and 2011

S. Risk Management

The Hospital is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. These risks are covered by commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

T. Subsequent Events

The Hospital considered events occurring through September 25, 2012 for recognition or disclosure in the financial statements as subsequent events. That date is the date the financial statements were available to be issued.

(2) Cash

The Hospital's deposits in banks at June 30, 2012 were entirely covered by federal depository insurance or the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Hospital is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentality's; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high-rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; and certain joint investment trusts, and warrants or improvement certificates of a drainage district.

Credit Risk: The Hospital's investments are categorized to give an indication of the level of risk assumed by the Hospital at year end. The Hospital's investments are all category 1 which means that the investments are insured or registered or the securities are held by the Hospital or its agent in the Hospital's name.

Interest Rate Risk: The Hospital's investment policy allows for the investment of funds with varying maturities as a means of managing its exposure to fair value losses arising from changes in interest rates, so long as the maturities are consistent with the needs and uses of the Hospital's funds.

Custodial credit risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Hospital's investment policy requires the fund to be deposited into banking institutions that have the ability to collateralize any deposits made in excess of the Federal Deposit Insurance Corporation's insurance limits.

Investment return, including return on assets limited as to use, for the years ended June 30, 2012 and 2011 is included in investment income on the Statements of Revenue, Expenses and Changes in Net Assets.

(3) Net Patient Service Revenue

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Notes to Financial Statements
June 30, 2012 and 2011

Medicare. Inpatient acute care services rendered to Medicare program beneficiaries in a Critical Access Hospital are paid based on Medicare defined costs of providing the services. Inpatient nonacute services and certain outpatient services related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2010.

Medicaid. Inpatient acute services and outpatient services rendered to Medicaid program beneficiaries in a Critical Access Hospital are paid based on Medicaid defined costs of providing the services. Physician clinic services are paid based on fee schedule amounts. The Hospital is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Hospital.

The Hospital has also entered into payment agreements with certain commercial insurance carriers. The basis for payment to the Hospital under these agreements primarily includes discounts from established charges.

The Hospital reports net patient service revenue at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

Revenue from the Medicare and Medicaid programs accounted for approximately 55% and 9%, respectively, of the Hospital's net patient revenue for the year ended June 30, 2012 compared to 53% and 6%, respectively in 2011. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

(4) Other Revenue

Other revenue for the years ended June 30, 2012 and 2011, consisted of the following:

| | <u>2012</u> | <u>2011</u> |
|--|-------------------|----------------|
| Services provided to clinic | \$ 400,479 | 427,643 |
| HRSA grant | 126,196 | 134,462 |
| State of Iowa electronic health records incentive payments | 78,219 | -- |
| Medical office building rent | 27,600 | 27,600 |
| Specialty clinic rent | 16,863 | 16,011 |
| Medical records transcript fee | 16,446 | 5,694 |
| MediMate | 12,771 | 13,765 |
| Purchasing rebates | 11,417 | 11,727 |
| Other | 7,592 | 37,777 |
| Meals | 7,496 | 6,202 |
| Occupational health consulting | 6,888 | 4,905 |
| Ambulance service fee billing revenue | 5,311 | -- |
| Vending | 2,845 | 1,613 |
| Wellness center dues | 1,826 | 1,990 |
| Cholesterol screening | 1,780 | 2,465 |
| | <u>\$ 723,729</u> | <u>691,854</u> |

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The Health Information Technology for Economic and Clinical Health Act contains specific financial incentives designed to accelerate the adoption of electronic health record (EHR) systems among health care providers. During 2012 the Hospital qualified for the financial incentives payments by attesting it met specific criteria set by the Center for Medicare and Medicaid services (CMS). Management's attestation is subject to audit by the federal government or its designee. The Iowa Department of Health and Human Services (DHHS) provides EHR incentive payments that will be earned and received through various payments through 2014. An incentive receivable of \$78,219 has been recognized in the balance sheet as of June 30, 2012 as part of other receivables. The amounts recognized are based on management's best estimates and are subject to change, which would be recognized in the period in which the change occurs.

(5) Composition of Patient Receivables

Patient receivables as of June 30, 2012 and 2011 consist of the following:

| | <u>2012</u> | <u>2011</u> |
|--|---------------------|------------------|
| Patient accounts receivable | \$ 2,466,197 | 1,281,250 |
| Less estimated third-party contractual adjustments | (166,538) | (84,491) |
| Less allowance for uncollectibles | <u>(808,619)</u> | <u>(276,786)</u> |
| | <u>\$ 1,491,040</u> | <u>919,973</u> |

The Hospital is located in Hawarden, Iowa. The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The approximate mix of receivables from patients and third-party payors was as follows:

| | <u>2012</u> | <u>2011</u> |
|--------------------------|-------------|-------------|
| Medicare | 40% | 28% |
| Medicaid | 6 | 5 |
| Blue Cross Blue Shield | 10 | 12 |
| Other third-party payors | 17 | 28 |
| Private pay | <u>27</u> | <u>27</u> |
| | <u>100%</u> | <u>100%</u> |

(6) Assets Limited as to Use

Cash deposits and investments designated by the Board for future capital improvements, and endowments as of June 30, 2012 and 2011, are summarized as follows:

| | <u>2012</u> | <u>2011</u> |
|---------------------------------------|-------------------|----------------|
| Capital Improvements and Endowments - | | |
| Cash and certificates of deposit | \$ <u>441,605</u> | <u>378,073</u> |

Cash deposits and investments restricted by donor for future capital improvements, and endowments as of June 30, 2012 and 2011, are summarized as follows:

| | <u>2012</u> | <u>2011</u> |
|---------------------------------------|------------------|---------------|
| Capital Improvements and Endowments - | | |
| Cash and certificates of deposit | \$ <u>99,973</u> | <u>99,712</u> |

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Notes to Financial Statements
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(7) Capital Assets, Net

Capital asset additions, retirements and balances as of June 30, 2012 and 2011, are summarized as follows:

| | <u>June 30, 2011</u> | <u>Additions</u> | <u>Transfers and Disposals</u> | <u>June 30, 2012</u> |
|--|--------------------------|------------------|------------------------------------|--------------------------|
| Capital assets, not being depreciated: | | | | |
| Land | \$ 234,912 | -- | -- | 234,912 |
| Construction in progress | 92,233 | 172,511 | -- | 264,744 |
| Total capital assets, not being depreciated | <u>327,145</u> | <u>172,511</u> | <u>--</u> | <u>499,656</u> |
| Capital assets, being depreciated: | | | | |
| Land improvements | 54,997 | -- | -- | 54,997 |
| Hospital buildings | 1,556,820 | -- | -- | 1,556,820 |
| Fixed equipment | 508,011 | 58,289 | -- | 566,300 |
| Major moveable equipment | 2,044,271 | 18,746 | -- | 2,063,017 |
| Total capital assets, being depreciated | <u>4,164,099</u> | <u>77,035</u> | <u>--</u> | <u>4,241,134</u> |
| Less accumulated depreciation: | | | | |
| Land improvements | 32,228 | 1,795 | -- | 34,023 |
| Hospital buildings | 1,124,253 | 38,377 | -- | 1,162,630 |
| Fixed equipment | 412,914 | 11,361 | -- | 424,275 |
| Major moveable equipment | 1,527,765 | 202,611 | -- | 1,730,376 |
| Total accumulated depreciation | <u>3,097,160</u> | <u>254,144</u> | <u>--</u> | <u>3,351,304</u> |
| Total capital assets, being depreciated, net | <u>1,066,939</u> | <u>(177,109)</u> | <u>--</u> | <u>889,830</u> |
| Total capital assets, net | <u>\$ 1,394,084</u> | <u>(4,598)</u> | <u>--</u> | <u>1,389,486</u> |
| | <u>June 30, 2010</u> | <u>Additions</u> | <u>Transfers and Disposals</u> | <u>June 30, 2011</u> |
| Capital assets, not being depreciated: | | | | |
| Land | \$ 19,384 | 215,528 | -- | 234,912 |
| Construction in progress | 31,201 | 87,240 | 26,208 | 92,233 |
| Total capital assets, not being depreciated | <u>50,585</u> | <u>302,768</u> | <u>26,208</u> | <u>327,145</u> |
| Capital assets, being depreciated: | | | | |
| Land improvements | 41,289 | 13,708 | -- | 54,997 |
| Hospital buildings | 1,556,820 | -- | -- | 1,556,820 |
| Fixed equipment | 511,595 | -- | 3,584 | 508,011 |
| Major moveable equipment | 1,903,860 | 148,744 | 8,333 | 2,044,271 |
| Total capital assets, being depreciated | <u>4,013,564</u> | <u>162,452</u> | <u>11,917</u> | <u>4,164,099</u> |
| Less accumulated depreciation: | | | | |
| Land improvements | 30,435 | 1,793 | -- | 32,228 |
| Hospital buildings | 1,085,875 | 38,378 | -- | 1,124,253 |
| Fixed equipment | 403,433 | 13,065 | 3,584 | 412,914 |
| Major moveable equipment | 1,264,906 | 271,192 | 8,333 | 1,527,765 |
| Total accumulated depreciation | <u>2,784,649</u> | <u>324,428</u> | <u>11,917</u> | <u>3,097,160</u> |
| Total capital assets, being depreciated, net | <u>1,228,915</u> | <u>(161,976)</u> | <u>--</u> | <u>1,066,939</u> |
| Total capital assets, net | <u>\$ 1,279,500</u> | <u>140,792</u> | <u>26,208</u> | <u>1,394,084</u> |

Construction in progress consists of computer software and other miscellaneous costs. These items are to be paid for out of operations.

Notes to Financial Statements
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(8) Mercy Accounts Payable

Mercy Accounts Payable includes amounts due to Mercy Medical Services and Mercy Medical Center related to the Hospital's portion of financial support for the Hawarden Mercy Medical Clinic and Ireton Community Clinic and other professional and management fees. Mercy accounts payable as of June 30, 2012 and 2011 is summarized as follows:

| | <u>2012</u> | <u>2011</u> |
|---|------------------|---------------|
| Mercy Medical Services for share of Hawarden Mercy Medical Clinic and Ireton Community Clinic operating support | \$ 24,027 | 29,168 |
| Mercy Medical Center for professional and management services | <u>30,460</u> | <u>26,995</u> |
| | <u>\$ 54,487</u> | <u>56,163</u> |

(9) Professional Liability Insurance

The Hospital carries a professional liability policy (including malpractice) providing coverage of \$1,000,000 for injuries per occurrence and \$3,000,000 aggregate coverage. In addition, the Hospital carries an umbrella policy which also provides \$1,000,000 per occurrence and aggregate coverage. These policies provide coverage on a claims-made basis covering only those claims which have occurred and are reported to the insurance company while the coverage is in force. In the event the Hospital should elect not to purchase insurance from the present carrier or the carrier should elect not to renew the policy, any unreported claims which occurred during the policy year may not be recoverable from the carrier.

Accounting principles generally accepted in the United States of America require a healthcare provider to recognize the ultimate costs of malpractice claims or similar contingent liabilities, which include costs associated with litigating or settling claims, when the incidents that give rise to the claims occur. The Health Center does evaluate all incidents and claims along with prior claim experienced to determine if a liability is to be recognized. For the years ending June 30, 2012 and 2011, management determined no liability should be recognized for asserted or unasserted claims. Management is not aware of any such claim that would have a material adverse impact on the accompanying financial statements.

(10) Employee Retirement and Defined Benefit Pension Plan

The Hospital contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by State statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa 50360-9117.

Plan members are required to contribute 5.38% of their annual salary and the Hospital is required to contribute 8.07% of annual covered payroll. Contribution requirements are established by State statute. The Hospital's contribution to IPERS for the years ended June 30, 2012, 2011 and 2010 were \$185,618, \$139,603, and \$123,484, respectively, equal to the required contributions for each year.

(11) Related Party Transactions

Effective January 1, 2005, the Hospital and Mercy Medical Services (MMS) entered into a joint venture whereby each partner has a 50% sponsorship interest in Hawarden Regional Healthcare Clinics, LLC. (HRHC). The Hospital and MMS share equally in the net income (loss) of HRHC. HRHC operates clinics in Hawarden and Ireton, Iowa.

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Notes to Financial Statements
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Hawarden Clinic

The Hospital's share of Hawarden Clinic's (HC) 2012 and 2011 operating loss was \$12,068 and \$109,580, respectively, and is included in joint venture loss, net in the accompanying statements of revenue, expenses and changes in net assets.

The Hospital hires the employees of HC and leases them back to HC. Amounts received by the Hospital for expenses paid in 2012 and 2011 was \$292,970 and \$328,013, respectively, and is included in the accompanying statements of revenue, expenses and changes in net assets. The Hospital also received management fees from HC totaling \$50,000 in 2012 and 2011, and monthly rent totaling \$27,600 for the years ended June 30, 2012 and 2011. These amounts are included in other revenue.

HC owed the Hospital \$404,381 and \$507,862 at June 30, 2012 and 2011, respectively. These amounts are recorded in due from related party on the balance sheets.

Ireton Clinic

The Hospital's share of Ireton Clinic's (IC) 2012 and 2011 operating loss was \$3,017 and \$13,284, respectively, and is included in joint venture loss, net in the accompanying statements of revenue, expenses and changes in net assets.

The Hospital hires the employees of IC and leases them back to IC. Amounts received by the Hospital for expenses paid in 2012 and 2011 was \$47,509 and \$39,630, respectively, and is included in the accompanying statements of revenue, expenses and changes in net assets. The Hospital also received management fees from IC totaling \$10,000 in 2012 and 2011. These fees are included in other revenue.

IC owed the Hospital \$6,683 and \$44,372 at June 30, 2012 and 2011, respectively. These amounts are recorded in due from related party on the balance sheets.

See Note 8 regarding amounts due Mercy Medical Services.

Patient Service Revenue
For the Years Ended June 30, 2012 and 2011

| | 2012 | | | | 2011 | | | |
|---|-------------------|-------------------|------------------|---------------------|------------------|-------------------|------------------|------------------|
| | <u>Inpatient</u> | <u>Outpatient</u> | <u>Swing Bed</u> | <u>Total</u> | <u>Inpatient</u> | <u>Outpatient</u> | <u>Swing Bed</u> | <u>Total</u> |
| NURSING SERVICES: | | | | | | | | |
| Medical, surgical and obstetrics | \$ 299,236 | 581,625 | -- | 880,861 | 218,750 | 254,136 | -- | 472,886 |
| Swing bed | -- | -- | 490,848 | 490,848 | -- | -- | 161,536 | 161,536 |
| Observation | -- | 57,808 | -- | 57,808 | -- | 83,002 | -- | 83,002 |
| | <u>299,236</u> | <u>639,433</u> | <u>490,848</u> | <u>1,429,517</u> | <u>218,750</u> | <u>337,138</u> | <u>161,536</u> | <u>717,424</u> |
| OTHER PROFESSIONAL SERVICES: | | | | | | | | |
| Radiology | 53,230 | 1,746,776 | 7,479 | 1,807,485 | 62,361 | 1,425,438 | 9,023 | 1,496,822 |
| Laboratory | 58,613 | 1,052,532 | 31,397 | 1,142,542 | 62,286 | 1,300,924 | 22,244 | 1,385,454 |
| Physical therapy | 8,484 | 670,245 | 76,133 | 754,862 | 8,739 | 660,317 | 31,292 | 700,348 |
| Pharmacy | 117,314 | 1,575,520 | 329,293 | 2,022,127 | 85,355 | 1,149,551 | 93,779 | 1,328,685 |
| Emergency and outpatient service | 5,819 | 752,681 | -- | 758,500 | 5,556 | 452,411 | -- | 457,967 |
| Professional fees | 56,845 | 335,284 | 9,211 | 401,340 | 27,555 | 287,708 | 2,959 | 318,222 |
| Gastro-Intestinal | -- | 202,326 | -- | 202,326 | -- | 156,037 | -- | 156,037 |
| Respiratory therapy | 48,537 | 57,978 | 26,277 | 132,792 | 60,279 | 61,004 | 38,756 | 160,039 |
| Electrocardiology | 16,257 | 134,998 | 1,400 | 152,655 | 5,200 | 117,862 | 600 | 123,662 |
| Central services and supply | 71,626 | 130,581 | 152,141 | 354,348 | 50,531 | 142,693 | 41,979 | 235,203 |
| Cardiac rehab | -- | 76,914 | -- | 76,914 | -- | 39,756 | -- | 39,756 |
| Occupational therapy | 857 | 24,685 | 14,959 | 40,501 | -- | 36,809 | 7,020 | 43,829 |
| Speech therapy | 1,069 | 15,993 | 1,581 | 18,643 | -- | 10,211 | 1,627 | 11,838 |
| Anesthesiology | -- | 36,767 | -- | 36,767 | -- | 20,582 | -- | 20,582 |
| Operating and recovery rooms | -- | 47,758 | -- | 47,758 | -- | 30,777 | -- | 30,777 |
| Dietary consulting | -- | 7,342 | -- | 7,342 | -- | 11,597 | -- | 11,597 |
| | <u>438,651</u> | <u>6,868,380</u> | <u>649,871</u> | <u>7,956,902</u> | <u>367,862</u> | <u>5,903,677</u> | <u>249,279</u> | <u>6,520,818</u> |
| GROSS PATIENT SERVICE REVENUE | <u>\$ 737,887</u> | <u>7,507,813</u> | <u>1,140,719</u> | <u>9,386,419</u> | <u>586,612</u> | <u>6,240,815</u> | <u>410,815</u> | <u>7,238,242</u> |
| LESS: | | | | | | | | |
| Contractual allowances and other deductions, primarily Medicare and Medicaid | | | | (2,130,974) | | | | (1,388,176) |
| Provision for bad debts | | | | (602,900) | | | | (204,560) |
| NET PATIENT SERVICE REVENUE | | | | <u>\$ 6,652,545</u> | | | | <u>5,645,506</u> |

See accompanying independent auditor's report

Other Operating Revenue
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|--|-------------------|----------------|
| Services provided to clinic | \$ 400,479 | 427,643 |
| HRSA grant | 126,196 | 134,462 |
| State of Iowa electronic health records incentive payments | 78,219 | -- |
| Medical office building rent | 27,600 | 27,600 |
| Specialty clinic rent | 16,863 | 16,011 |
| Medical records transcript fee | 16,446 | 5,694 |
| MediMate | 12,771 | 13,765 |
| Purchasing rebates | 11,417 | 11,727 |
| Other | 7,592 | 37,777 |
| Meals | 7,496 | 6,202 |
| Occupational health consulting | 6,888 | 4,905 |
| Ambulance service fee billing revenue | 5,311 | -- |
| Vending | 2,845 | 1,613 |
| Wellness center dues | 1,826 | 1,990 |
| Cholesterol screening | 1,780 | 2,465 |
| | <u>\$ 723,729</u> | <u>691,854</u> |

See accompanying independent auditor's report

Department Expenses
For the Years Ended June 30, 2012 and 2011

| | 2012 | | | | 2011 | | | |
|-------------------------------------|-----------------------|---|-----------------------|------------------|-----------------------|---|-----------------------|------------------|
| | Salaries and Wages | Professional Fees and Purchased Services | Supplies and Other | Total | Salaries and Wages | Professional Fees and Purchased Services | Supplies and Other | Total |
| NURSING SERVICES: | | | | | | | | |
| Medical and surgical | \$ 811,050 | 53,971 | 114,588 | 979,609 | 684,469 | 31,619 | 89,993 | 806,081 |
| Observation | 4,790 | -- | -- | 4,790 | 9,477 | -- | -- | 9,477 |
| | <u>815,840</u> | <u>53,971</u> | <u>114,588</u> | <u>984,399</u> | <u>693,946</u> | <u>31,619</u> | <u>89,993</u> | <u>815,558</u> |
| OTHER PROFESSIONAL SERVICES: | | | | | | | | |
| Physical therapy | 52,268 | 375,160 | 19,667 | 447,095 | 49,507 | 352,787 | 18,563 | 420,857 |
| Emergency room | 38,066 | 817,929 | 1,523 | 857,518 | 53,315 | 798,016 | 4,123 | 855,454 |
| Laboratory | 198,910 | 179,691 | 116,266 | 494,867 | 191,643 | 160,186 | 91,142 | 442,971 |
| Radiology | 78,535 | 235,717 | 18,459 | 332,711 | 65,208 | 198,509 | 16,858 | 280,575 |
| Hawarden community clinic | 248,046 | -- | -- | 248,046 | 286,517 | -- | 11,210 | 297,727 |
| Pharmacy | 4,737 | 35,844 | 561,146 | 601,727 | 3,950 | 34,749 | 352,568 | 391,267 |
| Medical records | 113,859 | 48,053 | 34,352 | 196,264 | 70,582 | 56,612 | 23,920 | 151,114 |
| Respiratory therapy | 423 | 13,150 | 5,739 | 19,312 | 523 | 16,819 | 481 | 17,823 |
| Outpatient clinic | 42,136 | -- | 523 | 42,659 | 34,069 | -- | 476 | 34,545 |
| Central services and supply | 1,842 | -- | 83,489 | 85,331 | 1,013 | -- | 48,555 | 49,568 |
| Gastro-Intestinal | 5,824 | -- | 22,588 | 28,412 | 6,483 | -- | 26,320 | 32,803 |
| Occupational therapy | -- | 41,393 | 1 | 41,394 | -- | 46,037 | 61 | 46,098 |
| Intravenous therapy | 27,633 | -- | -- | 27,633 | 19,664 | -- | -- | 19,664 |
| Electrocardiology | 1,755 | 4,977 | -- | 6,732 | 1,581 | 4,128 | -- | 5,709 |
| Cardiac rehab | 45,947 | -- | 5,490 | 51,437 | 40,674 | -- | 6,745 | 47,419 |
| Home health | -- | 8,424 | -- | 8,424 | -- | 12,150 | -- | 12,150 |
| Occupation health | 1,110 | -- | 1,500 | 2,610 | 251 | -- | 264 | 515 |
| Operating and recovery room | 772 | 8,921 | 1,786 | 11,479 | 2,350 | 8,231 | 3,752 | 14,333 |
| Anesthesiology | -- | 9,360 | -- | 9,360 | -- | 11,000 | -- | 11,000 |
| Speech therapy | -- | 31,674 | -- | 31,674 | -- | 23,670 | -- | 23,670 |
| Wellness center | -- | -- | -- | -- | -- | -- | 296 | 296 |
| | <u>861,863</u> | <u>1,810,293</u> | <u>872,529</u> | <u>3,544,685</u> | <u>827,330</u> | <u>1,722,894</u> | <u>605,334</u> | <u>3,155,558</u> |
| GENERAL SERVICES: | | | | | | | | |
| Plant operation and maintenance | 95,753 | -- | 125,734 | 221,487 | 69,017 | -- | 136,625 | 205,642 |
| Dietary | 122,709 | 3,750 | 31,032 | 157,491 | 114,767 | 2,950 | 20,951 | 138,668 |
| Housekeeping | 62,618 | -- | 14,424 | 77,042 | 48,880 | -- | 10,632 | 59,512 |
| Laundry and linen | -- | -- | 23,049 | 23,049 | 9,605 | -- | 15,139 | 24,744 |
| | <u>281,080</u> | <u>3,750</u> | <u>194,239</u> | <u>479,069</u> | <u>242,269</u> | <u>2,950</u> | <u>183,347</u> | <u>428,566</u> |
| ADMINISTRATIVE SERVICES | <u>309,964</u> | <u>285,541</u> | <u>73,004</u> | <u>668,509</u> | <u>301,279</u> | <u>330,884</u> | <u>105,141</u> | <u>737,304</u> |
| NONDEPARTMENTAL: | | | | | | | | |
| Employee benefits | -- | -- | 646,907 | 646,907 | -- | -- | 562,910 | 562,910 |
| Depreciation and amortization | -- | -- | 254,144 | 254,144 | -- | -- | 324,428 | 324,428 |
| Insurance | -- | -- | 70,369 | 70,369 | -- | -- | 63,430 | 63,430 |
| Interest | -- | -- | 671 | 671 | -- | -- | 6,247 | 6,247 |
| | <u>--</u> | <u>--</u> | <u>972,091</u> | <u>972,091</u> | <u>--</u> | <u>--</u> | <u>957,015</u> | <u>957,015</u> |
| GRAND TOTAL | <u>\$ 2,268,747</u> | <u>2,153,555</u> | <u>2,226,451</u> | <u>6,648,753</u> | <u>2,064,824</u> | <u>2,088,347</u> | <u>1,940,830</u> | <u>6,094,001</u> |

See accompanying independent auditor's report

Patient Receivables and Allowance for Doubtful Accounts
For the Years Ended June 30, 2012 and 2011

ANALYSIS OF AGING:

| Days Since Discharge | 2012 | | 2011 | |
|---------------------------------------|---------------------|------------------|------------------|------------------|
| | Amount | Percent of Total | Amount | Percent of Total |
| 0 - 30 | \$ 933,717 | 37.86 % | 646,919 | 50.49 % |
| 31 - 60 | 288,572 | 11.70 | 185,523 | 14.48 |
| 61 - 90 | 131,338 | 5.33 | 82,185 | 6.41 |
| 91 - 120 | 187,960 | 7.62 | 90,518 | 7.06 |
| Over 120 | 924,610 | 37.49 | 276,105 | 21.56 |
| | <u>2,466,197</u> | <u>100.00 %</u> | <u>1,281,250</u> | <u>100.00 %</u> |
| Less: | | | | |
| Allowance for doubtful accounts | (808,619) | | (276,786) | |
| Allowance for contractual adjustments | <u>(166,538)</u> | | <u>(84,491)</u> | |
| | <u>\$ 1,491,040</u> | | <u>919,973</u> | |

ALLOWANCE FOR DOUBTFUL ACCOUNTS:

| | 2011 | 2010 |
|---|-------------------|------------------|
| Balance, beginning of year | \$ 276,786 | 208,984 |
| Provision of uncollectible accounts | 602,900 | 204,560 |
| Recoveries of accounts previously written off | 23,169 | 11,642 |
| Accounts written off | <u>(94,236)</u> | <u>(148,400)</u> |
| Balance, end of year | <u>\$ 808,619</u> | <u>276,786</u> |

See accompanying independent auditor's report

Inventory/Prepaid Expenses
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|-----------------------|-------------------|----------------|
| INVENTORY: | | |
| Pharmacy drugs | \$ 83,847 | 63,284 |
| All other | <u>20,104</u> | <u>17,314</u> |
| | <u>\$ 103,951</u> | <u>80,598</u> |
| PREPAID EXPENSES: | | |
| Insurance | \$ 14,179 | 33,459 |
| Service Contracts | 64,788 | 64,051 |
| Dues | <u>10,942</u> | <u>7,034</u> |
| | <u>\$ 89,909</u> | <u>104,544</u> |

See accompanying independent auditor's report

Financial and Statistical Highlights
For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|---|--------------|--------------|
| Patient days: | | |
| Adult and pediatric - | | |
| Medicare | 263 | 183 |
| Other | <u>123</u> | <u>126</u> |
| | 386 | 309 |
| Swing bed | <u>857</u> | <u>296</u> |
| Total | <u>1,243</u> | <u>605</u> |
| Patient discharges: | | |
| Adult and pediatric - | | |
| Medicare | 79 | 74 |
| Other | <u>46</u> | <u>32</u> |
| | 125 | 106 |
| Swing bed | <u>53</u> | <u>31</u> |
| Total | <u>178</u> | <u>137</u> |
| Average length of stay: | | |
| Adult and pediatric - | | |
| Medicare | 3.3 days | 2.5 days |
| Other | 2.7 days | 3.9 days |
| Swing bed | 16.2 days | 9.5 days |
| Emergency room visits | 1,403 | 1,180 |
| Specialty clinic visits | 1,768 | 1,645 |
| Number of employees - full-time equivalents | | |
| Hospital | 44.36 | 42.40 |
| Clinic | <u>7.71</u> | <u>7.06</u> |
| | <u>52.07</u> | <u>49.46</u> |

**Independent Auditor's Report on Internal Control Over Financial Reporting and
on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with Government Auditing Standards**

To the Board of Trustees
Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
Hawarden, Iowa:

We have audited the financial statements of Hawarden Regional Healthcare (f/k/a Hawarden Community Hospital) (Hospital), as of June 30, 2012 and 2011, and have issued our report thereon dated September 25, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs as items II-A-12 and II-B-12 that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Hospital's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Comments involving statutory and other legal matters about the Hospital's operations for the year ended June 30, 2012, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Hospital. Since our audit was based on tests and samples, not all transactions that might have

had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes. Prior year statutory comment, items II-A-11 and II-B-11 have not been resolved.

This Hospital's responses to findings identified in our audit are described in the accompanying schedule of findings and questioned costs. While we have expressed our conclusions on the Hospital's responses, we did not audit the Hospital's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees, and constituents of the Hospital, and other parties to whom the Hospital may report. This report is not intended to and should not be used by anyone other than those specified parties.

SEIM JOHNSON, LLP

Omaha, Nebraska,
September 25, 2012.

Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

Part I: Summary of the Independent Auditor's Results

- a. An unqualified opinion was issued on the financial statements.
- b. Two reportable conditions in internal control over financial reporting were disclosed by the audit of the financial statements.
- c. The audit did not disclose any non-compliance which is material to the financial statements.

Part II: Findings Related to the Financial Statements

Instances of Non-Compliance:

No matters were reported.

Significant Deficiency

II-A-12

Management Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimations and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements. Audit journal entries were made to adjust amounts recorded by management for certain settlement, contractual adjustments in accounts receivable, and allowance for doubtful accounts estimates.

Recommendation: We recommend that management review their estimation processes in these areas and determine if additional procedures or templates can be added to enhance the estimation process at year end and on an interim basis.

Response: Management is aware of this deficiency and will develop additional procedures to improve the existing estimation process at year end and on an interim basis.

Conclusion: Response accepted.

Significant Deficiency

II-B-12

Segregation of Duties: One important aspect of internal controls is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The limited number of office personnel prevents a proper segregation of accounting functions necessary to assure optimal internal control.

Recommendation: Due to a limited number of administrative personnel, a lack of segregation of duties exists. Proper segregation of duties ensures an adequate internal control structure and, without this segregation, a greater risk of fraud and defalcation may exist. We recommend the Hospital continue to monitor and improve its segregation of duties.

Response: Management is aware of this deficiency in internal control and believes it is economically not feasible for the Hospital to employ additional personnel for the purpose of greater segregation of duties. The Hospital will continue to maintain and improve its segregation of duties.

Conclusion: Response accepted.

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

Part III: Other Findings Related to Required Statutory Reporting

Questionable Expenditure: We noted no expenditures that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

Travel Expense: No expenditures of Hospital money for travel expenses of spouses of Hospital officials and/or employees were noted.

Business Transactions: The following transactions between the Hospital and Hospital officials:

| | |
|---|------------------|
| Matt Hummel, Member Board of Trustees: | |
| Hospital pharmacy supervision fee | \$ 18,000 |
| Hospital purchased of drugs and supplies from Businesses operated by Matt Hummel - Booth Pharmacy | <u>3,690</u> |
| Total | \$ <u>21,690</u> |
| Glea Hamik, Member Board of Trustees: | |
| Wages paid for being a part-time employee during the year ended June 30, 2012 | \$ 32,497 |
| Food purchased from stores owned by spouse - Fiesta Foods | <u>11,492</u> |
| Total | \$ <u>43,988</u> |

Board Minutes: - No transactions were found that we believe should have been approved in the Board minutes but were not.

Deposits and Investments: We noted no instances of noncompliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa and the Hospital's investment policy.

Publishing Requirements: An annual condensed statement of total receipts and expenditures is to be published in a newspaper of the city in which the Hospital is located according to Chapter 392.6 of the Code of Iowa.

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Summary Schedule of Prior Year Audit Findings
For the Year Ended June 30, 2012

| Finding | Status | Corrective Action Plan or Other Explanation |
|----------------|---|--|
| II-A-11 | Net realizable value of accounts receivable and third party settlements | Unresolved, similar finding reported at II-A-12 |
| II-B-11 | Segregation of duties over accounting functions | Unresolved, similar finding reported at II-B-12 |

Hawarden Regional Healthcare
(f/k/a Hawarden Community Hospital)
A Component Unit of the City of Hawarden, Iowa

Audit Staff
For the Year Ended June 30, 2012

This audit was performed by:

- Brian D. Green, FHFMA, CPA, Partner
- Chase S. Manstedt, CPA, Staff Auditor
- J. Alex Morton, Staff Auditor